No. 15755

United States
COURT OF APPEALS
for the Ninth Circuit

MERRIMAN H. HOLTZ and HELENE TYROLL HOLTZ,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Petitioners' Reply Brief

Petition to Review a Decision of the Tax Court of the United States

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Petitioners submit, in reply to some of the contentions advanced in respondent's brief, the following:

(a) It is asserted in respondent's brief (pp. 11, 12) that the question of whether the bad debt losses under consideration herein were business or non-business bad debt losses is one of "pure fact for the trial court . . . " and that, accordingly, the only issue on appeal is whether the Tax Court's finding is clearly erroneous. A similar contention was made by the Commissioner of Internal Revenue in Washburn v. Commissioner of Internal Rev-

enue 51 F.2d 949 (8 Cir). At issue in the Washburn case was the question of whether or not taxpayer had suffered a net loss within the meaning of Section 204 of the Revenue Act of 1921 which provided for the carryover of net losses "resulting from the operation of any trade or business regularly carried on by the taxpayer . . . " In answer to the respondent's contention the Court stated, at p. 951: "That there may be some degree of finality in a finding of fact by an administrative body may be conceded, but such finding cannot take from the courts the power to construe a statute and determine whether it covers such a situation as the facts present. Great Northern Ry. Co. v. Merchant's Elevator Co., 259 U.S. 285, 42 S. Ct. 477, 66 L. Ed. 943. In our judgment there is nothing in the point urged by the respondent that we are concluded by the decision of the Board (of Tax Appeals, now the Tax Court of the United States) because of its finding as an ultimate fact that petitioner was not engaged in a trade or business regularly carried on."

The primary facts involved in the case at bar have been stipulated by the parties hereto. Any determination by the Tax Court can only be considered as a conclusion of law determined by applying the relevant statutes to the stipulated facts—the findings of the Tax Court are made in support of this legal conclusion and the question to be determined is whether the facts bring the bad debt loss of petitioner within the concepts of a business bad debt or a non-business bad debt as those concepts were intended by the Congress when it enacted Sections 23 (k)(1) and 23(k)(4) of the Internal Revenue Code of

1939. Manifestly, this is a question involving the construction of a statute, and, as such, is one for determination by this Court.

(b) Petitioners do not contend, as alleged in respondent's brief (pp. 15, 16) that "any taxpayer who carries on business through corporations" is entitled to a business bad debt deduction for advances to the corporations that subsequently become worthless. Petitioners' contention is that where an individual's trade or business is carried on through several controlled corporations, and the individual's business activities for a 20 year period consist almost entirely of the organizing, acquiring, managing and financing of such corporations, that a loss suffered in connection with such activity is of a business nature and is not a non-business loss.

(c) Putnam v. Commissioner, 352 U.S. 82, to which reference is made in respondent's brief at page 16, involved a bad debt loss suffered by an attorney, as guarantor of a corporate obligation, in a venture not connected with his law practice. The taxpayer's contention, before the Supreme Court of the United States, was that the loss suffered by him was incurred in a transaction entered into for profit, though not connected with his trade or business, and deductible as a loss pursuant to Section 23(e)(2), Internal Revenue Code of 1939.* The

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"Section 23. DEDUCTIONS FROM GROSS INCOME.

"In computing net income there shall be allowed as deductions: * * * * *

"(e) LOSSES BY INDIVIDUALS.

"In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—* * *

"(2) if incurred in any transaction entered into for profit, though not connected with the trade or business * * * * * *."

Court held that the loss suffered was a non-business bad debt, deductible under the provisions of Section 23(k)(4). The disparity between the facts in Putnam and those of the instant case are obvious: the taxpayer in Putnam was an attorney and the corporation whose loan he guaranteed had *no connection* with the taxpayer's law practice; petitioner Merriman H. Holtz's guaranties were made on behalf of corporations, the organizing, managing and financing of which constituted the petitioner's *primary* business activity for a period of twenty years.

(d) To describe the portion of the House Ways and Means Committee's Report quoted in petitioner's brief at p. 8 as "an incidental observation" (Resp. Br., p. 16) does not change what appears to be a clear expression of the legislative intent with respect to Section 23(k)(4). The Congressional Committee obviously was describing the purpose of its proposed legislation. It does not seem reasonable to assume, as does respondent, that the quoted portion of the Committee Report was not properly descriptive of the Committee's *primary objective* in proposing the legislation in question, but was, instead, merely an "incidental observation."

(e) Respondent seeks to distinguish the instant case from Giblin v. Commissioner 227 F.2d 692, Washburn v. Commissioner 51 F.2d 949 and Campbell v. Commissioner 11 TC 510, by pointing out that in each of the cited cases, all of which were decided favorably to the taxpayers, the taxpayers had promoted or organized eleven or twelve corporations (Resp. Br., p. 18). It is submitted once again that if a determination is to be made as to whether petitioner's activities fall within the

scope of the business of organizing, financing and managing business enterprises, the quantitative test which respondent applies cannot logically be limited to the *organization* of corporations and the number so organized but must likewise be applied to the financing and managing activities of the taxpayer. With respect to the quantity of financing transactions (Ex. 5E, 6F, 7G, 8H, 9I, 10J) and the extent of corporate managerial activity, it is submitted that the record clearly discloses that petitioner Merriman H. Holtz is entitled to even more favorable consideration than were the taxpayers in Giblin, Washburn or Campbell, supra.

Respectfully submitted,

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